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PROGRAMME OF WORK OF THE INTERGOVERNMENTAL WORKING GROUP OF EXPERTS ON INTERNATIONAL STANDARDS OF ACCOUNTING AND REPORTING: DISCUSSION OF ACCOUNTING ISSUES ARISING DURING PRIVATIZATION, INCLUDING INDIVIDUAL COUNTRY CASE-STUDIES

Accounting problems arising during privatization in Mexico

Report of the Secretary-General

SUMMARY

The Government of Mexico believes that the country has developed to the point where many business enterprises should be transferred to the private sector to promote efficiency and expansion. For basic industries such as minerals extraction, utilities and transportation, control can be achieved by regulation instead of government ownership and operation. Trade sales through a bidding process and share flotations have been the primary methods used by the Government to attain its objectives to date. Specific transactions are handled by one of the commercial banks within the country as designated by the Ministry of Finance and Public Credit. Accounting standards and the auditing profession are well established in Mexico. Because of hyperinflation in recent years, however, historical financial information used for the valuation

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of companies has had to be adjusted by general price indices or expert appraisals. Banks and other financial institutions in Mexico use accounting principles in accordance with government requirements for their respective industries that are not in accordance with international standards. This problem has yet to be overcome. Also, proper accruals for environmental liabilities and potential obligations to terminated staff are matters that must be considered for every entity that is being privatized.

The following case-study is based on a written contribution by the Ministry of Finance and Public Credit of Mexico.

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INTRODUCTION

1. Since taking office, the present federal Government has focused its efforts on modernizing the country in all areas and improving the quality of life of the Mexican people. The National Development Plan for 1989-1994 contains the strategy formulated to guide those efforts.

2. With regard to public enterprises in particular, a modernization programme has been implemented that includes the privatization of non-strategic publicly owned entities. The aim is for a more democratic and more efficient State. Historically, different entities grew out of various situations that had resulted from the belief at the time in a need for State participation to support the country's development. Under conditions of macroeconomic stability, Mexico experienced an important transformation of its economic and productive sectors, as a result of a comprehensive policy of structural change.

3. There are a number of general considerations that have to be taken into account in order to understand the evolution of the public sector. The strengthening and consolidation of the institutions acquired by the Government at different stages of the country's development led to the creation of public enterprises or agencies to perform some of the functions that the Constitution had entrusted to the State, such as the stabilization of the national economic system and the promotion of the system's development. For example, the following were established: the Bank of Mexico, a network of development banks, the National Securities Commission and the National Banking and Insurance Commission. Some entities were set up in order to exploit strategic natural resources for the nation's benefit, produce raw materials widely used in industry and agriculture or provide the population with basic services. This was the case for enterprises such as Petróleos Mexicanos, the Federal Electricity Commission, Ferrocarriles Nacionales, Altos Hornos de México and Fertilizantes Mexicanos, among others. Other entities were set up at the initiative of the development banks, in particular the National Finance Bank, throughout the 50-year period. Projects were also promoted to eliminate bottlenecks at various stages of the country's development, produce substitutes for imports, increase export capacity, encourage the modernization of plants and generally stimulate and complement investments in the social and private sectors. From this promotional work emerged such entities as the Sidermax complex (iron and steel companies) and the capital goods industries.

4. In the same way, the public sector was also increasing the number of publicly owned enterprises by acquiring or taking over a number of companies that had originally been set up by the private sector but could not operate satisfactorily or productively. Thus, in order to protect jobs and maintain the production facilities, the State incorporated into the public sector enterprises from very different and varied economic branches, for example, State-owned commercial fisheries and sugar refineries. Other entities were created or established in order to achieve the specific goals of social welfare. They included all the institutes in the health sector and the

Compañía Nacional de Subsistencias Populares (National Staple Foods Corporation).

5. The situation described above reflects a great variety of goals that gave rise to direct participation of the State in industry, trade and services. It is useful to point out that in Mexico the reasons for that participation were very similar to those that led to the establishment of public enterprises in other countries of the world.

6. Although there was flexibility in the establishment of public enterprises there was little flexibility in removing public enterprises from the public sector once the purposes for which they had been created were achieved. This imbalance, added to the accelerated growth of the public sector in certain periods, resulted in adverse situations that limited the development of the enterprises themselves, impairing their efficiency and effectiveness in terms of both their own management and their contribution to national objectives. The result was participation in economic activities that, more extensive than selective, made institutional coordination more difficult and consequently reduced the impact of the activities of those enterprises on the national economy. At the end of 1982, the State was participating in 45 branches of economic activity through 1,155 publicly owned entities, covering such diverse manufacturing areas as woolen fabrics, soft drinks, chinaware and bicycles.

7. On the other hand, this situation made possible the attempt to pursue many different objectives with a single instrument - public enterprise. However, taken as a whole, regulation of the market, granting of subsidies, creation of jobs, promotion of technology and exports, coverage of the market and support for other public enterprises were objectives that were often difficult to achieve satisfactorily in the administration of publicly owned enterprises. Sometimes the result was the financial, administrative and operational weakening of the enterprises themselves.

I. OBJECTIVES OF PRIVATIZATION

8. The difficult financial situation of the federal government resulting from the general economic conditions of recent years highlighted the urgent need to secure greater rationality and efficiency in publicly owned enterprises. Towards the end of 1982, the government department responsible for the public sector called for structural changes to (a) streamline the State's role in economic activities, (b) strengthen control by eliminating elements of secondary importance and concentrate on what was fundamental and necessary, (c) consolidate the position of those enterprises in which the State was to retain a role and (d) extend the framework of a mixed market economy. The economic crisis confronting the country in the early 1980s, the weaker financial position of the State and the shortage of resources for many publicly owned entities created the need to devise and implement a policy to secure concentration of the federal government's resources in the strategic areas defined in the Constitution and in the priority areas demanded by economic policy.

II. IMPLEMENTATION OF THE PRIVATIZATION PROCESS

A. Form of privatization

9. The scaling-down of the public sector entails not only the sale of enterprises but also the consideration of other options: merger, reduction of operations, transfer and winding-up. The selection of one of these options depended on the specific situation of the enterprise at the time that the decision to privatize was made. Entities that had already achieved their goals or were not economically viable were wound up or had their operations curtailed. Enterprises were merged in order to improve the use of their resources for various purposes, such as marketing and activities complementary to the production process. As set forth in the National Development Plan for 1989-1994, State Governments were given control of priority enterprises of regional or local importance for their development programmes, and enterprises were sold if they were not strategic or priority enterprises and there was some benefit in their acquisition by the social or private sectors.

B. Legal framework

10. The legislative and juridical basis for the privatization of publicly owned entities is the Political Constitution of the United Mexican States. In accordance with article 134 of the Constitution, the divestment of publicly owned entities has usually been carried out by public competitive bidding in order to ensure the best terms of sale for the State in regard to price, timing and other relevant matters. In addition, capital has been raised through public offerings of securities on the domestic and international exchanges. The section of the present study entitled "Special cases" includes a description of the recent highly successful flotation of shares of Teléfonos de México (TELMEX).

11. Articles 25 and 28 of the Constitution set forth the strategic areas for government control and establish the framework within which the State will collaborate with the social and private sectors to promote and to organize development activities.

12. The Federal Law on Public Entities, dated 14 May 1986, sets out the fundamental provisions governing the relations between the central and public sectors within a framework of greater managerial freedom. In the exercise of his regulatory powers, the President of the Republic issued the Regulations for the Federal Law on Public Enterprises. The Regulations published on 26 January 1990 in the Official Gazette, were established to govern the creation, organization, operation, control and closure of public entities.

13. The privatization of public entities has to be kept in line with the forecasts in the federal budget. For public entities created by the Congress, the Congress's prior authorization is also required. The transfer process, in addition to being based on the laws and regulations mentioned above, is guided by the procedures that the Inter-Ministerial Commission on Expenditure drew up

for this purpose. This Commission is a collegial body comprising the Ministry of Finance and Public Credit, the Ministry of Planning and Budget, the Office of the Controller-General of the Federation, the Ministry of Trade and Industrial Development, the Ministry of Labour and Social Security and the Bank of Mexico. The Ministry of Finance and Public Credit is responsible for coordinating, supervising and implementing the sale of publicly owned companies. 1/

14. With a view towards strengthening the action of the federal Government in the sale of public companies, the President of the Republic has, by decree, created the Privatization Unit for Publicly Owned Entities within the Ministry of Finance and Public Credit. This Unit consists of six persons at the management level, together with supporting staff.

15. To support these actions, a total reform of the financial sector of the economy was undertaken as well. The availability of capital both domestic and foreign was increased by a programme to strengthen and modernize the financial sector that was adopted in 1989. These measures applied mainly to the banking sector and to the stock market, and among the many measures taken were an increase in the minimum capitalization required for financial intermediaries, creation of private pension funds, increase in the maturity dates of government securities, a reserve requirement for banks of 30 per cent of deposits, permission for banks to place their certificates of deposit on the secondary market, privatization of State banks, liberalization of interest rates, elimination of automatic credit lines to certain sectors and creation of deposit insurance.

C. Methods

16. The process of privatization by means of the sale of companies is extemely broad and complex but many of the formalities are the same for all companies, irrespective of their size. The procedures followed in the transfer of state-owned entities are described below.

D. Steps for privatization

1. Proposal of the coordinating agency

17. The process is formally initiated when the ministry that bears responsibility for the industry sector, considering that the company in question is neither a priority nor of strategic importance, presents its proposal for privatization to the Inter-Ministerial Commission on Expenditure. For example, if a hotel were involved, the proposal would be a matter for the Ministry of Tourism; but a sugar mill-related proposal would be a matter for the Ministry of Agriculture and Water Resources.

2. Opinion of the Inter-Ministerial Commission on Expenditure

18. The Inter-Ministerial Commission on Expenditure analyses the proposal and, depending on the company's general situation, economic sector and operational background, determines the most appropriate form of privatization. As mentioned above, that may be winding-up, reduction of operations, merger, transfer or sale.

3. Privatization agreement

19. If it is decided that the company is to be sold, the Ministry of Planning and Budget, pursuant to its mandate, 2/ sends an official communication to the Ministry of Finance and Public Credit to start the sales process.

4. Designation of the agent bank

20. The Ministry of Finance and Public Credit, in all cases, designates one of the country's 18 commercial banks to act as sales agent for the federal Government. The decision as to which particular bank will conduct the sale depends on its experience and workload. The Privatization Unit for Publicly Owned Entities of the Ministry of Finance and Public Credit analyses the situation of the individual company and, in coordination with the designated agent bank, develops the sales plan.

5. Features of the sale

21. Once the sales plan has been prepared and approved and the characteristics and specific situation of the company established, the agent bank proposes to the Ministry of Finance and Public Credit general guidelines for the sale. Among the most important matters are: convening of meetings, conditions of sale, timetable of activities, profile of the enterprise, prospectus and amount of the deposit to be received. All of these matters require the final approval of the Privatization Unit for Publicly Owned Entities.

6. Sales profile and prospectus

22. The agent bank prepares two documents. The first is an informational profile, which is a brief document describing the general characteristics of the company. At this time an advertisement is published in the major local newspapers informing interested parties that the company is for sale and that they can obtain preliminary information. The second document is the descriptive prospectus containing the most relevant information on the company, including such items as financial statements, labour situation and general business operations. In order to obtain the prospectus it is necessary, in the majority of cases, to deposit an amount whose size varies

according to the size of the company. A written commitment to maintain confidentiality (specifying that any information received will not be divulged during a specific period of time) is also required. In addition, interested parties are invited to pay a technical visit to the company.

7. Technical-financial appraisal

23. On the basis of the information provided by the company, the agent bank, employing a variety of methods, prepares a study, referred to as the technical-financial appraisal or valuation. Financial measurements frequently presented are equity value (that is, the value of net assets or assets less liabilities), current value of future cash flows, liquidation value and market value. The results of this analysis will provide a minimum indicative value, which will be employed as a yardstick in considering offers, of the enterprise's worth. The company may be sold for a different amount, depending on market conditions. Generally speaking, such appraisals are made by national experts but in certain cases, if the situation so requires, the opinion of international experts may be requested. Mexican companies that have used such international services include: Compañía Mexicana de Aviación, S.A. de C.V., Teléfonos de México, S.A. de C.V., Compañía Minera Cananea, S.A., Siderúrgica Lázaro Cárdenas Las Truchas, S.A., and Altos Hornos de México, S.A.

24. Of all the transactions carried out by the current Administration, 88 per cent (121 enterprises) involved transfers at a price equal to or greater than the recommended minimum amount, while only 12 per cent (17 enterprises) were sold for lower amounts. Most of the enterprises that were sold for less than their appraised value were sugar refineries. In such cases, the operating conditions encountered, labour and financial problems, and the unpredictability of sugar cane and sugar prices had led to judgements that the value of those enterprises was lower than originally projected.

8. Assessment of bids

25. In accordance with the principles for sales, the agent bank receives the bids in a sealed envelope. This takes place with the greatest possible transparency in the presence of a notary public and of representatives from the Ministry of Finance and Public Credit and the Office of the Controller-General of the Federation. Afterwards, the Institute of Credit standardizes the bids so as to facilitate comparison. When a bid is analysed, the plans of the purchaser with regard to the enterprise are taken into account, as well as the price of the transaction and conditions of payment. It is important for the federal Government to know the future investment and employment plans of the purchaser. Nevertheless, the most important consideration in the assessment is the price.

26. The sales agent bases his or her recommendation to the Ministry of Finance and Public Credit on the proposal guaranteeing the most favourable

conditions of sale for the State. In the event that all bids are below the recommended minimum amount or only one bid is submitted, the results obtained are set out before the Inter-Ministerial Commission on Expenditure and the Commission makes a decision, either designating a purchaser or, if there is no suitable bidder, reopening the bidding. In general, enterprises are offered for bid three times, and if a favourable result if not obtained, on the specific authorization of the Inter-Ministerial Commission on Expenditure direct negotiations are held with the interested party or parties and representatives of the Office of the Controller-General of the Federation.

9. Authorization and decision on sale

27. When the judgement of the Inter-Ministerial Commission on Expenditure is favourable, the Ministry of Finance and Public Credit issues an official note of authorization and decision of sale in favour of the most favourable bid for the State.

10. Formalization of the sale

28. The unit owning the federal Government's shares and the purchaser sign the contract of sale, thus formalizing the transaction. The purchaser then carries out a buyer's audit which is submitted for consideration to the Ministry of Finance and Public Credit, and if any claims are made and accepted, the relevant amounts are disbursed. The proceeds of the sale are deposited in the Treasury of the Federation in accordance with the contract of sale. The Ministry of Finance and Public Credit sends to the Ministry of Planning and Budget and to the Controller-General at the Federation an official note to begin the formal deletion of the enterprise from the group of public bodies (attaching copies of the contract of sale and the payment to the Treasury of the Federation).

11. Compiling the "white book"

29. When the sale has been concluded the agent bank is responsible for preparing a document called the white book, which is a collection of all of the official documents related to each stage of the transfer process. The Coordinator of the Privatization Unit for Publicly Owned Entities sends the white book to the Ministry of Planning and Budget, the Ministry having responsibility for the industry sector, and the Office of the Controller-General of the Federation so that, in accordance with the powers conferred on that Office, it can monitor and oversee the privatization processes. In addition, a copy is sent to the accounting office of the chamber of deputies so that an expert body can make appropriate valuations of the enterprises sold.

E. Special cases

30. As explained earlier, these are the general procedures for the transfer of public companies. There are, however, other arrangements for specific enterprises that require special strategies for such sales. The following cases are examples.

Compañía Mexicana de Aviación

31. In the case of this airline an option was sought that would spare the Government the expense of having to meet from its own resources enormous investment requirements and would at the same time develop the enterprise and obtain for the Government a fair price for its shares. It was decided that the mechanism of capital infusion, by which the proceedings of the sale would not be deposited in the Treasury of the Federation but employed to capitalize the enterprise, would be used. With this strategy the State promoted the growth and modernization of Mexicana de Aviación, and the resources that it did not have to transfer to that public company were channelled into other high-priority expenditure items. The enterprise was capitalized at $140 million.

Fisheries

32. A scheme was devised to fit the particular characteristics of fisheries and to provide for participation in the enterprises of private financial agents through capital investment companies (SINCAS). This proposal and the criteria governing the scheme were authorized by the Inter-Ministerial Commission on Expenditure and, as in the other transfer processes, depended on the support of the agent bank working together with a brokerage house. Under this scheme the transfer processes have been concluded for four fisheries in two packages, the first package comprising Pesquera del Pacífico, S.A. de C.V., and Productos Pesqueros de Topolobampo, S.A. de C.V., and the second, Productos Pesqueros de Siunaloa, S.A. de C.V., and Productos Pesqueros de Matanacitas, S.A. de C.V.

Sugar refineries

33. Most of the sugar refineries privatized during the present Administration had been operating at a loss for recent sugar harvests and the rate of return had been lower than the national average. In order to encourage the sale, balanced packages were created and a payment scheme designed that was based on bonds pegged to the price of sugar. Just like all the other transfer processes, the sales were formalized with the conclusion of a contract of sale. In this case, a cash payment of 20 per cent was made when the contract was signed and the remaining 80 per cent was paid through issuance of the above-mentioned bonds. Sixteen sugar refineries have now been privatized under this arrangement.

Teléfonos de México (TELMEX) 3/

34. In order to privatize Teléfonos de México, the government authority responsible for the industry sector first proposed pursuing the following objectives which were identified by the President of the Republic:

(a) A substantial improvement in service;

(b) Steady expansion of the existing system;

(c) Strengthening of research and technological development;

(d) The guarantee of the rights of workers and of their share in the equity of the enterprise;

(e) The guarantee that Mexicans would hold a controlling interest in the entity.

35. In order to fulfil the first three objectives, updated programmes were needed for the expansion, improvement and modernization of the telephone system and for the undertaking of industrial and technological research that would increase the competitiveness of the enterprise and of the country in the field of telecommunications. TELMEX would have to increase its number of lines by an estimated annual average of 12 per cent between 1990 and 1994. By 1995, every village with more than 500 inhabitants should have at least one long-distance public telephone. By 1995, public telephone kiosks should be installed with a density of 5 kiosks for every 1,000 inhabitants. By the year 2000, the waiting time for the installation of new service lines in cities with a population of more than 5,000 should be reduced to one month.

36. At the same time, the concession from the Government provides for detailed quality-of-service goals, the designation of a councillor by the Ministry of Communications and Transport until August 1993 and the introduction of a system of rate regulation through price ceilings. The concession, which went into operation in 1991, provides that TELMEX service rates will be subject to a price ceiling in real terms on its basic telephone service package.

37. A substantial amount of new capital was necessary if the objectives of the government authority were to be accomplished. The securities market represented an efficient alternative for financing productive investment. In this sense, the market has gained new importance in Mexico's current economic development and was also felt to be an ideal vehicle for attracting foreign resources through portfolio investment, as well as a key instrument in the privatization process of government enterprises. Thus, a decision was reached to raise this capital through a very large equity shares flotation.

38. The process was planned in two stages. The first stage involved financial arrangements for the divestiture of the company, based on a restructuring of its capital stock through declaration of a dividend in new

shares series L with limited voting rights, and several legal procedures to maximize the liquidity of those shares and their acceptance in world markets. Through this mechanism, the control package, represented by series A shares equivalent to 20.4 per cent of the total capital, was put together. In a public auction in December 1990, this package was assigned to Grupo Industrial Carso, a Mexican holding company associated with Southwestern Bell Telephone of the United States of America and France Telecom. The second stage consisted in the public offering of series L shares, which the Mexican Government had received as a dividend for its participation in the company.

39. Owing to its nature, this transaction required the standardization of legal and accounting principles in the markets that were participating in the process, in this case, the New York Stock Exchange (United States) and the Bolsa Mexicana de Valores (Mexico). The objective of the Mexican authorities in the international offering was to provide equal opportunities to all participants. Owing to differences in the public offering processes of the United States and Mexico, the following basic principles were established:

(a) Full and timely disclosure of information regarding the issue;

(b) Simultaneous pricing of the offering;

(c) Coordinated initiation of transactions in the secondary market.

40. Because the majority of shares were placed in the United States, close collaboration between the Mexican and United States Securities Commissions was required to establish the mechanisms necessary to successfully incorporate the TELMEX L shares in the major world markets.

41. During the offering period, the distribution in Mexico of a preliminary prospectus in Spanish (the so-called red herring) was authorized as a new practice in the Mexican market that provided for the disclosure to all potential investors of comparable information at the same time.

42. The underwriters for the offering were commercial banks (government-owned at the time) in Mexico, and Mexico's industrial development bank, Nacional Financiera. It was recognized that the participation of these institutions in the securities market should be carried out independently from their main shareholder, the federal Government, which in this particular case was the entity offering the shares.

43. During the selling period, it was necessary to reconcile and coordinate a great number of regulations and practices of several countries for the global offering that was being made.

44. The placement was completed just a few hours after having been initiated, causing the underwriting syndicate to dissolve the very first day. The Mexican Government received two payments: $375 million, representing 138 million shares placed on the Mexican stock exchange and the sale of 150 million shares for the TELMEX union workers' fund, and $1.79 billion

resulting from the placement of 1.515 billion L shares in the United States, Europe, Canada, Japan and the rest of the world. The total offering amounted to $2.17 billion.

National credit institutions

45. A presidential agreement established the principles and bases of the process of privatizing national credit institutions and commercial banking institutions. The Bank Privatization Committee, presided over by the Ministry of Finance and Public Credit, was established for that purpose. 4/ In view of the technical details and complexity of the bank privatization process, the Committee designed, subject to the provisions of the presidential agreement, an integrated sales scheme in three stages: valuation of institutions, registration and authorization of possible purchasers and transfer of shares held by the federal Government. To implement the first stage, the Committee decided upon two valuations: one to be undertaken by the banks themselves, supported by various consultants or investment banks and the other to be done by consultants commissioned by the Committee. To that end, it engaged the services of prominent national and international consultants possessing broad experience in the field of banking systems who were also collaborating in the preparation of sales prospectuses.

F. Impact of privatization

46. The human and financial resources that were released as a result of streamlining the State's role in the economy have been redeployed to priority areas. Privatization has contributed to industrial modernization efforts and to the effective and appropriate exercise of State supervision within the new realities of national and international markets and strengthened the State's capacity to meet the social service demands of the population. Mexico's experience with the transfer of public companies has been satisfactory in terms of both the number of entities sold and the transparency, efficiency and strict legal integrity of the transactions concluded.

47. As of May 1991, 826 enterprises had been privatized (including 141 sold to the private sector), 138 were in the process of privatization and 264 remained in State ownership. The sales to the private sector (primarily to Mexican citizens) raised $Mex 16.6 trillion (US$ 5.5 billion) for the Treasury. Of all the transactions carried out by the current Government, 86 per cent (121 enterprises) involved transfers at a price equal to or greater than the recommended minimum amount, while only 12 per cent (17 enterprises) involved sales for lower amounts. Most of the enterprises that were sold for less than their appraised value were sugar refineries. In those cases, the operating conditions encountered, labour and financial problems, and the unpredictability of sugar cane and sugar prices led to judgements that the value of the refineries was lower than originally projected.

48. Unquestionably, the simplest stage of the programme has been completed, since the smallest companies have been privatized. However, the experience

acquired in that process has created the necessary conditions for dealing with more complex cases, including companies that have had to undergo extensive restructuring not only of their financial systems, but also of their operations. The privatization of public entities has been included as one component of the economic modernization that is intended to help meet primary national objectives.

49. As a result of privatization, the Government now focuses more attention on basic issues, promoting the social infrastructure and responding more efficiently to the demands of the population. The Government also consolidates and fulfils its constitutional duties and gives highest priority to national development to guarantee a better quality of life for Mexican citizens.

III. IMPLICATIONS OF PRIVATIZATION FOR ACCOUNTING

A. Existing accounting practices

50. In general, all public companies follow accounting practices that are consistent with accrual accounting. Businesses outside the financial sector, for example, Teléfonos de México (TELMEX) and Altos Hornos, use a business accounting system based on the accounting principles promulgated by the Mexican Institute of Public Accountants (IMCP). IMCP principles are consistent with those promulgated by the Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting (ISAR) and by the International Accounting Standards Committee. In the financial sectors, banks, investment firms and insurance companies employ accounting systems based on government regulations that differ from IMCP principles.

51. The privatization of banking institutions is now in progress; consequently, ways of adapting the accounting system to IMCP principles and hence to international standards are being studied. No problems arise when companies outside the financial sector are privatized provided that their practices comply with international standards.

52. The accounting systems of public corporations are very complex since they must provide the following information:

(a) Budgetary accounting required by the federal Government;

(b) Management accounting required by management;

(c) Financial accounting for the audits that must be conducted by the Controller-General or an independent public accountant;

(d) Tax accounting for the payment of taxes.

53. In the light of the foregoing, the administrative burden connected with the accounting system is considerably lightened when a company moves from the public sector to the private sector.

B. Financial information

54. Since 1979 Mexico has had an effective accounting standard for dealing with inflation. Given the rate of inflation in Mexico in recent years, financial information should be adjusted through either general price indices or expert valuation reports. The assets of non-financial-sector businesses previously owned by the Government are appraised using the general price index. However, banks utilize appraisals by in-house experts. (In the private sector they must always be independent experts.)

55. As a rule, appraisals are made by public accountants or expert appraisers registered with the National Securities Appraisal Commission, a unit of the Ministry of Finance and Public Credit. In order to practise public accounting, an individual must hold a licence that is recognized by the Ministry of Public Education, belong to an association of professional accountants and satisfy the requirements of a continuing education programme. To be accredited as an expert by the National Securities Appraisal Commission, an individual must hold the diploma of ingeniero and have specialized studies in some specific area.

C. Submission of accounting information

1. With regard to public sector companies undergoing privatization

56. Banks must bring their financial statements into line with international standards since their present accounting practices are not consistent with such standards. Other State-owned companies need to make only a few changes to conform to international standards. In all cases, companies need to revalue their assets to replacement cost. As for trade marks and other intellectual property rights, the country has had little experience in the valuation of such intangible assets. Businesses have almost no assets under this heading except amounts specified by national and international standards.

57. Regarding the estimation of liabilities, two problems arise, one relating to environmental pollution and the other to staff terminations. Pollution problems have led to the issuance of new standards and rules regulating economic activities; as a result, companies have been forced to make investments in equipment, relocations or changes in processes that in the normal course of operations they would not have considered.

58. In Mexico an employee who is dismissed is entitled to a seniority bonus, which is an amount equal to as much as 20 days per year of service, plus three months pay. There are no mandatory pension schemes. A number of banks have benefit plans that include these features, but in all other companies there is no provision for recording liability (though some have a bonus feature) because the amount cannot be accurately quantified and, if the employee has been dismissed justifiably, no payment is required. Nevertheless, when a company with staff having above-average seniority is sold, provisions are made for liability to be taken into account in the sales transaction.

59. The standards established by the National Banking Commission are currently being phased out in favour of IMCP accounting standards, which will bring the Commission's standards into line with international standards. In that connection, only IMCP standards are recognized in circulars of the Commission relating to financial information. It should be noted that, as in other countries, the accounting standards must be met in order to enable the National Banking Commission to perform its functions of control and supervision. Banks must overhaul their accounting systems in order to comply with generally accepted accounting standards and National Banking Commission rules. In the case of State-owned companies other than banks, there is a need to simplify the chart of accounts in order to eliminate budgetary control by Government.

D. Improving the audit function

60. The Office of the Controller-General of the Federation and the Ministry of Finance and Public Credit require a financial audit of companies in the public sector regardless of whether those entities have enough internal staff resources with the requisite skills for that purpose. In addition to financial auditing, standards for operational auditing are being tested. Financial auditing is performed according to rules established by IMCP. Those rules are fully consistent with the standards of the International Federation of Accountants (IFAC).

61. The Mexican Institute of Public Accountants sets standards for:

(a) Auditing;

(b) A code of professional ethics;

(c) Continuing education.

62. An example of the accounting activities related to a large privatization undertaking occurs in the case of a large public utility, Teléfonos de México, S.A., which was sold via an equity share flotation. The company applied IMCP accounting standards both before and after privatization and was registered on the New York Stock Exchange, where the United States Securities and Exchange Commission (SEC) accepted financial statements based on generally accepted accounting principles as understood in Mexico and only required that reconciliation be effected in the notes to the financial statements in order to make such statements conform to generally accepted American accounting principles. Financial statements prepared in accordance with Mexican principles have also been accepted for the registration of bonds that were issued in Europe.

63. In conclusion, Mexico has technical resources in accounting that are regarded as satisfactory, that is, (a) resources are committed to all levels of education, (b) national and international accounting standards are followed, (c) national and international auditing standards are adhered to and

(d) a professional organization steadfastly promotes professionalism and continuing education (in the Republic of Mexico there are 50 colleges affiliated with IMCP). As was noted above, the basic problem in connection with accounting standards lies with the financial sector - banks, brokerage firms and insurance companies, which continue to follow their own industry accounting rules. Those companies are not able to provide financial information in accordance with international standards.

Notes

1/ Procedures for the Transfer to the Social or Private Sectors for Valuable Consideration of Securities Representing the Equity of the Federal Government or any Public Entity in Companies in which the State Holds a Controlling Interest (September 1990).

2/ See article 32 of the Charter of the Federal Civil Service, and articles 32 and 68 of the Federal Law on Public Entities.

3/ The information on TELMEX is based on a presentation by the Chairman of the National Securities Commission of Mexico at the Sixteenth Annual Conference of the International Organization of Securities Commissions (Washington, D.C., 1991).

4/ See the Official Gazette, 25 September 1990.